Service Date: June 1, 1978

BEFORE THE UTILITY DIVISION
DEPARTMENT OF PUBLIC SERVICE REGULATION
MONTANA PUBLIC SERVICE COMMISSION

IN THE MATTER OF the Petition of MONTANA-DAKOTA UTILITIES COMPANY for Increased Rates and Charges in Gas Service to industrial customers.	)	UTILITY DIVISION DOCKET NO. 6509 ORDER NO. 4359a

Appearances:

Lester H. Loble, II, Attorney at Law, 833 North Last Chance Gulch, Helena, Montana 59601, appearing on behalf of the Applicant.

Intervenors:

John C. Doubek, Attorney at Law, 34 West Sixth Avenue, Helena, Montana 59601, appearing on behalf of the Montana Consumer Counsel, Geoffrey L. Brazier.

Carolyn S. Hazel, Attorney at Law, Box 2197, Houston, Texas, appearing on behalf of Continental Oil Corporation.

C. William Leaphart, Attorney at Law, 1 North Last Chance Gulch, Helena, Montana 59601, appearing on behalf of Great Western Sugar Corporation.

Jerome Anderson, Attorney at Law, Transwestern Life Building, Billings, Montana 59101, appearing on behalf of Lovell Clay Products, Pierce Packing and Midland Empire Companies.

For The Commission:

Dennis R. Lopach, Attorney at Law, 1227 Eleventh Avenue, Helena, Montana 59601, appearing for the Commission staff.

Frank E. Buckley, Administrator, Utility Division

Dan Elliott, C.P.A., Utility Division

Before:

Gordon E. Bollinger, Chairman and Presiding Officer
Thomas J. Schneider, Commissioner
P.J. Gilfeather, Commissioner
James R. Shea, Commissioner

FINDINGS OF FACT

General

1. Montana-Dakota Utilities Co. (MDU or Applicant) is a Delaware corporation furnishing electric and natural gas service to customers in the State of Montana. As a public utility, MDU's rates to its retail customers and the quality and conditions of its service are subject to the regulatory jurisdiction of the Montana Public Service Commission (Commission).

2. On June 1, 1977, MDU filed an application for authority to increase natural gas rates to its Montana industrial customers from 97.8 cents per-Mcf at 14.73 p.s.i.a. to $1.00 per Mcf. The application, which included the supporting written testimony of three witnesses, sought authority to institute an industrial rate tariff (Schedule 85-M-3) in place of the individual industrial contracts under which MDU had traditionally operated. Conditions of service, although not rates, would remain subject to individual contracts. The application also requested approval of a purchased gas adjustment clause for industrial customers.

3. On June 23, 1977, MDU filed a [lotion in this Docket requesting approval of the $1.00 rate on a temporary basis. The Motion was granted by Order No. 4359 on June 28, 1977. Pursuant to R.C.M. 1947, Sec. 70-113, revenues collected under this

interim order are subject to rebate if this order, the final order in this Docket, determines a lesser revenue level to be justified.

4. On September 1, 1977, pursuant to notice, a prehearing conference in this Docket was conducted in the offices of the Commission in Helena. Present, in addition to staff counsel, were Lester H. Loble II, representing Applicant; C. W. Leaphart, Jr., representing Great Western Sugar Co. (GW); and Jerome Anderson, representing Pierce Packing Co., Midland Empire Packing Co. and Lovell Clay Products (LCP). All parties represented at this conference agreed that discovery could be handled informally, relieving the Commission of the burden of establishing formal discovery vehicles and timetables.

5. A procedural order fixing prehearing procedures and deadlines, as well as the date of hearing, was served by the Commission on September 2, 1977.

6. On September 19, 1977, Continental Oil Corporation (Continental) filed a petition to intervene in this Docket. The petition was granted by the Commission on September 27, 1977.

7. A public hearing in this Docket was conducted in Helena, pursuant to published notice, on December 6, 1977. At the opening of the hearing, GW moved to dismiss the application, on the ground MDU was unlawfully seeking to discriminate against its industrial customers.

8. On December 20, 1977, MDU withdrew its request for a purchased gas adjustment clause as a part of its application. This withdrawal was accepted on December 30, 1977.

Revenue Requirement

9. MDU last sought a general natural gas rate increase in Docket No. 6441. The increase approved in that Docket applied, as MDU requested, to all customers other than the industrial class. Much discussion is contained in the post-hearing briefs about the fact the Docket No. 6441 increases did not apply to industrials, and the fact that this application applies only to industrials. Additionally, MDU seeks to utilize a number of the Commission's findings in Docket No. 6441 (Order No. 4369), based on an adjusted 1975 test year, to show a revenue need in this proceeding.

10. MDU witness Donald R. Ball performed a series of allocations of Applicant's 1976 revenues, expenses and investment to Montana operations. Mr. Ball acknowledged that he had allocated MDU's "raw" 1976 operating results, without analyzing the component parts of the revenue and expense totals in order to determine if adjustments were required for rate-making purposes. Accordingly, Mr. Ball was unable to assure the Commission that non-recurring expenses or institutional and promotional advertising expenses had not been allocated to Montana, (Tr. 78).

11. Mr. Gamble, MDU's Assistant Treasurer, took the allocated results developed by Mr. Ball and applied them to a year-end 1976 rate base. This process showed Applicant earning a 7.91% rate of return in 1976 on its gas utility in Montana. A late filed exhibit showed that applying the allocated 1976 results to an average rate base for 1976 would produce a rate of return of 8.03%.

12. Mr. Gamble argued, and his exhibits purported to show, that approval of the application would not result in excessive revenues for his firm. He argued that MDU would not and could not

exceed the 8.66% return allowed by the Commission in Docket No. 6441.

13. Because the 1976 results, which were the beginning point of MDU's revenue requirement methodology, have not been analyzed in order to determine which items should be adjusted for ratemaking purposes, the Commission does not agree with Mr. Gamble that the Docket No. 6441 return cannot be exceeded. Without such an analysis, Mr. Gamble's conclusion appears to be nothing more than an educated guess.

14. The MDU approach used to determine revenue requirement contains certain theoretical problems. For example, the 8.66% rate of return was determined appropriate for a 1975 test year in Docket No. 6441. MDU now applies that return to its 1976 results with no showing that the costs of its several capital components, are unchanged. The Commission finds that, on balance, and in view of the entire record, the revenue need methodology presented here is inherently weak, and must be rejected.

Proposed Distribution of Revenue Increase to Industrial Class

15. MDU's Mr. Gamble took the position that the revenue increase should be applied to the industrial customers only. This position was, he said, premised on his judgment that certain "value of service" considerations justified such a treatment. Some of MDU's industrial customers who intervened in this case took a very different view of the proposed revenue allocation, while others appeared to accept it.

16. Mr. Gamble acknowledged that the most recent allocated cost of service studies performed for MDU's gas utility (in conjunction with Docket No. 6441) showed the industrial class to

be contributing a return substantially in excess of the system average return (Tr. 118-119). Gamble argued that cost of service to the industrial customer should not be the sole determinant of the industrial price, however. The industrial customer should be asked to pay a rate which more closely approximates the cost of the gas with which MDU is replacing its existing supplies (Tr. 99). This "replacement price" standard, Gamble said, more closely measured the industrial class' fair share of total gas utility revenues. He also contended that the "fair share" had been approached only within the past several years (Tr. 99).

17. Cost of replacement gas was but one factor of "value of service" pricing mentioned in Gamble's testimony. Other factors included the relative cost of alternative fuels, ease of conversion to alternative fuels, and quite simply, the customer's need for the product (Tr. 100). Weighing these and additional value of service considerations, and keeping in mind the cost of serving the industrial class, Gamble concluded that, in his judgment, industrial customers should be paying a higher rate.

18. Testimony in opposition to the rate increase was presented by Mr. M. C. Lamb, Director of Sales for Continental. Mr. Lamb generally contended that cost of service was the most reliable and widely-accepted pricing standard available to the Commission, and that vague assertions regarding value of service should not be relied upon.

19. Ralph Stewart, Jr., President and General Manager of Lovell Clay Products, testified in opposition to the proposed purchased gas adjustment clause. Mr. Stewart specifically stated that he was not opposed to the proposed price increase (Tr. 57).

20. Applicant has presented value of service evidence which is well-reasoned and based in logic. Industrial customers, as a group, are in a far better position to convert from natural gas to alternative fuels than are other customer classes. These customers have access to necessary capital, and represent a sufficiently high volume of usage to enable them to secure long term fuel supplies at a relatively low cost. Additionally, these customers enjoy other inherent benefits not available to the other customer classes, such as an ability to pass rate increases on to their customers, and tax deductions for utility payments.

21. In this proceeding, however, Applicant has not demonstrated a need for the additional revenue requested. The mix and match approach taken with regard to test year, rate base and rate of return do not provide the conclusive evidence needed for the Commission to increase rates. Viewed in this light, the proposed 2.2 cents per Mcf increase to industrial customers is denied. The Commission, in this case, distinguishes the mini hearing approach, used in the cost of purchased gas cases where the single issue of an expense account is examined, from a revenue request based upon the need for an increase justified in a fully developed rate hearing.

22. A rate tariff is an appropriate means under which a utility can serve its industrial customers, and the Commission endorses this approach to industrial service. A tariff should provide greater uniformity of treatment-than was formerly the case when contracts were, in effect, used as tariffs for the individual customers.

23. GW's Motion to Dismiss is discussion, deemed without merit, and is denied.

CONCLUSIONS OF LAW

1. The rate levels and rate structures resulting from the operation of this Order are just and reasonable.

ORDER

THE MONTANA PUBLIC SERVICE COMMISSION ORDERS THAT:

1. Applicant shall file an industrial rate tariff for its natural gas customers which reflects a base rate of 97.8 cents per Mcf at 14.73 p.s.i.a., the rate in effect prior to Order No. 4359. This tariff shall remain in effect until changed by order of the Commission.

2. Revenues collected under temporary Order No. 4359a are ordered rebated to MDU's industrial customers with ten percent (10%) interest from the time of their collection.

3. All motions and objections not ruled upon at the hearing are denied.

DONE IN OPEN SESSION at a meeting of the Montana Public Service Commission held May 31, 1978 by a vote of 4 - 0.

BY ORDER OF THE PUBLIC SERVICE COMMISSION:

GORDON E. BOLLINGER, Chairman

P. J. Gilfeather, Commissioner

THOMAS J. SCHNEIDER, Commissioner

JAMES R. SHEA, Commissioner

ATTEST:

Madeline L. Cottrill
Commission Secretary

(SEAL)

NOTE: You are entitled to judicial review of the final decision in this matter. If no Motion for Reconsideration is filed, judicial review may be obtained by filing a petition for review within thirty (30) days from the service of this order. If a Motion for Re consideration is filed, a Commission order is final for purpose of appeal upon the entry of a ruling on that motion, or upon the passage of ten (10) days following the filing of that motion. cf. the Montana Administrative Procedure Act, esp. Sec. 82-4216, R.C.M. 1947; and Commission Rules of Practice and Procedure, esp. 38-2.2(64)-P2750, ARM.

Service Date: June 20, 1978

BEFORE THE UTILITY DIVISION

DEPARTMENT OF PUBLIC SERVICE REGULATION

MONTANA PUBLIC SERVICE COMMISSION

* * * * *

IN THE MATTER of the Application of MONTANA-DAKOTA UTILITIES CO. for Increased Rates and Charges in Gas Service to Industrial Customers.	DOCKET NO. 6509 ORDER NO. 4359a

ERRATA SHEET TO
ORDER NO. 4359a

Order paragraph No. 1 should read:

1. Applicant shall file an industrial rate tariff for its natural gas customers which reflects a base rate of $1.027 cents per Mcf at 14.73 p.s.i.a. This tariff shall remain in effect until changed by order of the Commission.